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BP Negotiates a Deal in Russia

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risky place to invest, the nation's huge oil reserves—the seventh-largest in the world—come at some of the lowest prices of any in the world. This is tempting to the Western world's largest oil companies, which face problems trying to increase their oil and gas production, in part because of a lack of profitable investment opportunities around the globe.

Exxon Mobil Corp., the world's biggest publicly traded oil company, plans to spend a hefty $10 billion a year over the next 10 years to explore and develop new oil reserves, focusing especially on West Africa. And Royal Dutch/Shell Group, which last week warned that its oil and gas output would remain flat in 2003, expects soon to approve a multibillion-dollar investment to boost development of reserves in Sakhalin, in Russia's Far East.

Attracted by its cheap reserves, BP gambled on Russia in the late 1990s and got badly burned. The company had to write off $200 million of an investment. Now company officials feel the experience left them better prepared to put new money into the country. BP, which repeatedly missed its world-wide oil-and-gas production-growth targets last year, has been carrying out a broad review of its energy holdings and plans to announce a revised strategy for the company tomorrow. The company, which had 2001 revenues of $175 billion, operates mainly in North America and Europe, and is developing new deposits in Africa, the Caspian Sea and elsewhere.

A BP deal could prompt other Russian oil companies to consider selling stakes to foreigners now, when world oil prices may be peaking on fears of an Iraq war. Analysts say regime change in Iraq and an end to sanctions could reduce Russia's attractiveness to international oil companies.

BP has been negotiating the Russian deal for more than a year. The reserves it is eyeing are in Western Siberia, centrally located between established markets in Western Europe and the potentially huge growth market in China. People familiar with the matter said the parties closed in on an agreement this weekend. Under terms being discussed, BP's total investment could comprise a mixture of cash and its existing assets in Russia, they said. These assets, which include BP's Sidanko stake and interests in gasoline stations and a natural-gas field, are believed to be valued at less than $1 billion.

The new Russian company, which hasn't been named, would produce about 1.1 million barrels of oil a day, compared with BP's own daily output of 1.9 million barrels, and hold an estimated 10.6 billion barrels of oil reserves, compared with BP's 8.2 billion barrels.

A BP spokesman in Moscow would say only "we are still in discussions about the possibility of bringing" the companies together. None of the parties would comment on details.

Lord Browne is believed to be negotiating directly with several businessmen—Mikhail Fridman, Viktor Vekselberg and Len Blavatnik. Analysts believe they own most of TNK International and Sidanko, though the companies don't disclose their shareholders. None of the men returned calls seeking comment.

These Russian businessmen are the same that BP accused of cheating it just a few years ago. In 1997, BP paid $484 million for 10% of Sidanko, an investment that quickly soured when TNK's shareholders launched a bid to seize Sidanko's best oil fields. The opponents spent two years in a vicious legal battle, a dispute that helped frighten other foreign investors away from Russia.

The parties settled the conflict in 2001, after BP sought to lobby the U.S. Export-Import Bank to cut off a loan to TNK. Under the settlement, TNK returned the oil fields and bought a majority stake in Sidanko. The Russians gave BP the right to manage Sidanko, and BP last year bought another 15% of the company.

People familiar with the current talks say the parties have taken nearly a year as both sides have attempted to build up trust. In the new deal, BP wants to own a big-enough stake to have real influence but not a majority stake that would arouse local hostility and force BP to negotiate its own way in Russia.

Making Russia work for BP has been something of a personal project for BP's Lord Browne. He put his prestige on the line with his first Sidanko investment in 1997 and was furious when it went sour. "I've always considered America is governed by laws, not men," Mr. Browne told The Wall Street Journal in 2000, during the dispute. "The reverse may be true in Russia."

The sale of a big chunk of Russia's most important industry to BP would strengthen the reputation of the oligarchs who control swaths of Russian industry. In the mid-1990s, these powerful businessmen used their clout to buy the biggest oil and metals companies from the state on the cheap, and then milked them for profit without investing much. Lately, these businessmen's reputations have improved as they've begun investing more and sparking a boom in oil output. Shrewdly, they've also invested heavily in public relations.

Shares in the biggest Russia producers, OAO Lukoil and OAO Yukos, trade on Western stock exchanges. TNK International doesn't trade publicly, but shares in a subsidiary, Tyumen Oil Co., are listed in Russia and have risen in recent days amid rumors of the BP talks.

TNK's messy structure has complicated the negotiations. It also owns an oil producer called OAO Onako. And late last year TNK teamed up with a competitor, OAO Sibneft, to buy a big state-owned oil company called OAO Slavneft. TNK and Sibneft must decide how to divide that asset before the BP deal can be completed.

—Anita Raghavan contributed to this article.

Drawn by Russia's Oil Wealth, BP Negotiates a Big Investment

By JEANNE WHALEN
And BHUSHAN BAHREE

MOSCOW—Underlining the growing importance the West attaches to Russia's vast petroleum reserves, BP PLC is negotiating to invest as much as $4.5 billion in an oil giant that would be formed from merging three Russian companies, according to people familiar with the situation.

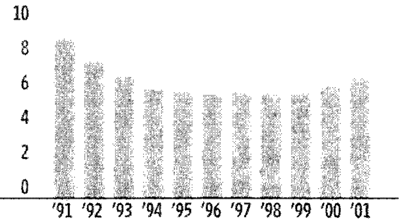
The proposed transaction would bring together Siberian oil producer OAO Sidanko, of which BP currently owns 25%, and two other oil companies owned by TNK International, these people said. They said London-based BP, one of the world's largest oil concerns, would acquire between a third and half of the new company, which would become the No. 3 oil producer in Russia behind OAO Yukos and OAO Lukoil, and a top-10 player globally. Details of the deal could be announced as early as this week, although the talks aren't yet complete and the terms could change.

The move comes as Western nations are seeking to reduce their dependence on oil exports from the Middle East, particularly as tensions in the region flare up ahead of a possible U.S.-led war in Iraq. Russia, the world's second largest oil producer after Saudi Arabia, is viewed as a significant source of additional oil for Western markets. But Russia's limited number of pipelines and deep-water ports to accommodate tankers have restricted exports. Rampant corruption in recent years also has kept Western investment at bay.

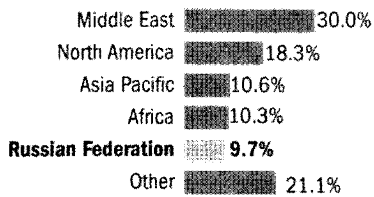
The BP transaction would mark the largest-ever foreign equity investment in Russia and could signal a renewed interest among Western companies in doing business there. Russia attracted less than a tenth of the $50 billion in foreign direct investment that China did last year. Yet the BP negotiations show that perceptions are improving. BP executives say President Vladimir Putin's

Climbing Back

Russian Federation's average daily oil production, in millions of barrels



2001 oil production by region, in percent



Source: BP

warming relations with the West have helped create a more-stable environment for foreign investors. And a few other deals have been clinched of late, including a commitment by a U.K. investor to spend as much as $500 million to acquire a stake in an aluminum concern.

Thanks to Russia's reputation as a

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